No. 86-49

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

AMERICAN ELECTRIC POWER COMPANY, INC., et al.,
Petitioners,

v.

KENTUCKY PUBLIC SERVICE COMMISSION, et al.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE KENTUCKY PUBLIC SERVICE COMMISSION IN OPPOSITION TO PETITION

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QUESTION PRESENTED

Whether the lower courts' unpublished decisions properly abstained from considering utility companies' challenges to a Kentucky Public Service Commission rate order when the utilities have brought the same attack on the same order with the same claims in state court and to the Federal Energy Regulatory Commission.

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OPINIONS AND ORDERS BELOW

The *per curiam* opinion of the Court of Appeals is unpublished and is reproduced in the Appendix to the Petition (Pet. App. 1a-12a).[1] The Court of Appeals' order denying petitioners' motion for rehearing is unpublished and is reproduced in the Appendix (Pet. App. 13a). The Court of Appeals' order denying petitioners' and the Federal Energy Regulatory Commission's motions to publish its decision is unpublished and is reproduced in the Appendix (Pet. App. 14a). The opinion of the District Court is unpublished and reproduced in the Appendix (Pet. App. 15a-23a).

JURISDICTION

The Court of Appeals entered its opinion and judgment on March 24, 1986 (Pet. App. 1a-12a). The Court of Appeals unanimously denied a timely petition for rehearing on May 6, 1986 (Pet. App. 13a). Petitioners assert jurisdiction under 28 U.S.C. §1254(1).

[1]References to the Appendix to the Petition for a Writ of Certiorari are cited as (Pet. App.).

STATEMENT

The lower courts' unpublished decisions abstained from adjudicating petitioners' challenges to a rate order of the Kentucky Public Service Commission (the "Commission") since petitioners simultaneously presented the same challenges to a state court and to the Federal Energy Regulatory Commission ("FERC"). The state court has affirmed the Commission on the merits and petitioners' appeal to a higher state court is pending. In the meantime, FERC has scheduled a public hearing on the matter.

1. Petitioner, American Electric Power Company, Inc. ("AEP"), is a holding company of electric power utilities. The remaining six petitioners, including Kentucky Power Company ("Kentucky Power"), are operating subsidiaries of AEP. Petitioners sell electricity in seven different states. Kentucky Power sells electricity to retail customers in Kentucky and is the only petitioner subject to the jurisdiction of the Kentucky Public Service Commission.

Kentucky Power and AEP's other principal subsidiaries are parties to an Interconnection Agreement providing for sharing of their electrical generating capacity. This agreement creates a pool of electricity and permits a member utility to draw from the pool when its customer's needs exceed its own generating capacity. The Interconnection Agreement, as modified by the FERC in 1979, provides that such "deficit" members may purchase available power from the pool by the payment of an "equalization charge" to the "surplus members" based on the average embedded generation costs of the surplus members. *Ohio Power Company*, 8 FERC ¶ 61,068 (CCH) (1979) *affirmed Ohio Power Company*, v. *FERC*, 668 F.2d 880 (6th Cir. 1982).[2]

In July 1978, Kentucky Power sought permission from the Commission to acquire a fifteen percent (15%) ownership interest in two large electricity generating units then being constructed by

[2]FERC approved the payment formula proposed by AEP despite its recognition that, with the cancellation of proposed new generation facilities (including one in which Kentucky Power would have been part owner), some of the AEP operating company members of the pool would remain in a deficit position for an indefinite period. *See* 8 FERC (CCH) ¶ 61,068 at p. 61,234.

another AEP subsidiary in Rockport, Indiana. The Commission denied authorization finding that Kentucky Power could purchase any needed additional power from the pool under the Interconnection Agreement.

In 1981, Kentucky Power again sought permission from the Commission to buy a 15% interest in the Rockport facility, claiming need for more generating capacity and that the Rockport facility was the only alternative available. On August 2, 1984, the Commission again denied Kentucky Power's request. The Commission rejected Kentucky Power's contentions that it could not continue to meet its needs by purchasing capacity from the pool under the Interconnection Agreement and that the Interconnection Agreement contained an implied obligation requiring Kentucky Power to buy a 15% share of the Rockport facility.

Rather than seeking judicial review of the Commission's decision, Kentucky Power promptly entered into a new agreement (the "Unit Power Agreement") with an AEP affiliate whereby Kentucky Power agreed to buy 15% of the annual output of the Rockport facility (thus, in effect securing the 15% interest in Rockport that the Commission had precluded it from owning).

The Unit Power Agreement was then filed with FERC as a jurisdictional rate schedule for the sale of electric power in interstate commerce for resale. *See* 16 U.S.C. § 824d(c). On October 1, 1984, FERC set the filing for hearing to determine the just and reasonableness of the rates. In its hearing order the FERC ruled that the "Kentucky Commission has jurisdiction to consider the appropriateness of [Kentucky Power's] acquisition of new facilities . . . ," and that there is ". . . no overlap or conflict . . ." between the roles of the federal and state agencies. *AEP Generating Co.*, 29 FERC (CCH) ¶ 61,002 (1984). On rehearing, on November 21, 1984, FERC ruled that while it did not believe consideration of Kentucky Power's prudence in making the purchase was relevant to the proceeding it had instituted to determine whether the filed rate for the Unit Power Agreement was just and reasonable, questions of whether a utility purchaser of capacity "has purchased wisely or made the best deal available" are "legitimate concerns of the state Commissions and this Commission as well [in cases

involving the wholesale rates of the purchaser] in determining whether purchases reflect prudently incurred expenses for purposes of determining the purchasers' rates for sale to others." *AEP Generating Co.*, 29 FERC (CCH) ¶ 61,246 at p. 61,501.

2. On December 4, 1984, the Commission, in a retail rate proceeding initiated by Kentucky Power, ruled that the utility had acted imprudently in buying the Rockport unit power because it could secure the additional capacity and energy to meet its customers' demands from the Interconnection Agreement pool at an annual cost savings of $23 million.

Kentucky Power then sought judicial review of the Commission's order in the state courts. At the same time, along with the other petitioners, it sought declaratory and injunctive relief in federal district court. Kentucky Power subsequently filed a petition with FERC for a declaratory ruling that power was not available to it under the Interconnection Agreement.

The Franklin County Kentucky Circuit Court, a designated state created forum with special expertise in the public utility regulation field,[3] affirmed the decision of the Kentucky Public Service Commission on March 24, 1986.[4] The state court found, among other things, that (1) the Interconnection Agreement does not require Kentucky Power to buy power from the Rockport facility at its higher incremental price and (2) the Interconnection Agreement allows Kentucky Power to purchase needed power from the AEP pool. And, the court also held that the Commission acted within its authority in considering the prudence of Kentucky Power's purchase. Kentucky Power's appeal to the state court of appeals is pending.

In the meantime, on January 16, 1985, the federal district court, by an unpublished decision, refused to enjoin the state proceedings, electing instead to abstain in favor of the state action. It relied on *Younger* v. *Harris*, 401 U.S. 37 (1971) and *Burford* v. *Sun Oil Co.*, 319 U.S. 315 (1943) (Pet. App. 19a-23a).

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[3]KRS Chapter 278.410(1).

[4]A copy of the state court's decision is attached hereto for the Court's convenience (Addendum 1a-6a).

On March 24, 1986, the Sixth Circuit affirmed, holding that the district court properly abstained. The unpublished *per curiam* decision held that *Younger* v. *Harris* required abstention (Pet. App. 6a-7a). Finding that "the regulation of consumer electric rates is an important state interest," that petitioners "will have an adequate opportunity to raise their federal claims in the pending state action," and that petitioners do not "claim that the Kentucky Commission's orders are the result of bad faith or harassment," the court of appeals ruled (*id.*):

> when the regulatory activities of the state proceed to a state judicial forum, the principles of comity and federalism that underly the *Younger* doctrine come into play and the federal courts should abstain from interfering.

The *per curiam* decision rejected abstention under the *Burford* doctrine (Pet. App. 4a-6a). However, the court of appeals' panel, comprised of two circuit judges and one district judge sitting by designation, voted two to one in favor of abstention on each theory.

The court of appeals thereafter denied a petition for rehearing. No active judge of the Sixth Circuit requested a vote on the suggestion for rehearing *en banc* (Pet. App. 13a). The court of appeals also denied motions filed by petitioners and by FERC for publication of the court of appeals' decision.

On August 20, 1986, after petitioners filed their petition for a writ of certiorari, FERC ruled on Kentucky Power's petition for a declaratory ruling, which was filed on November 18, 1985. FERC's orders, attached hereto as an Addendum (pp. 7a-27a), set for public hearing the issue as to the availability of power to Kentucky Power under the Interconnection Agreement. And FERC has required its administrative law judge to render a decision within ninety (90) days.

DISCUSSION

Petitioners contend (Petition p. 8) that the lower courts' unpublished decisions present "[t]he question whether abstention

principles deprive federal district courts of authority to prevent state utility commissions from interfering with the exclusive jurisdiction of FERC" which "has become one of the most important and frequently recurring questions facing the federal judiciary." However, this case does not involve a state utility commission that has interfered with FERC in any way. Instead, FERC had expressly held that the state commission had jurisdiction to pass on the prudence of Kentucky Power's purchases under the Unit Power Agreement.[5] And all of the issues as to the alleged invalidity of the Commission's order raised by petitioners before the federal district court also were raised, and resolved against Kentucky Power, in the state court in which it also sought relief. In addition, FERC has now instituted proceedings to determine the availability of power to Kentucky Power under the Interconnection Agreement. Nor do the lower courts' unpublished decisions as to the application of the *Younger* and *Burford* abstention doctrines present any substantial questions independently justifying review by this Court, Accordingly, the petition should be denied.

1. The petition presents a misleadingly narrow recitation of the factual background. This case does not present the problem of the proper role of the federal courts where it is alleged that a state commission has refused to follow rate orders approved by FERC. Instead, we have here a petitioner that sought to have a federal district court enjoin a state commission determination that a utility seeking a retail rate increase had acted imprudently by purchasing power costing more than the alternative power available to it under another rate schedule on file with FERC. FERC fully agreed with

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[5]As indicated in the Petition, questions have also been raised in both the state and federal courts as to the part of the Commission's rate order limiting the costs of certain high voltage transmission lines constructed by Kentucky Power to be included in its retail rate base to the level the Commission found to have been incurred for the benefit of Kentucky customers. As the Franklin Circuit Court's opinion makes clear (Addendum 3a-5a), there is no merit to petitioner's suggestion that their action conflicts with a pending rate proceeding initiated by petitioner before the FERC to allocate the costs of all AEP system high voltage transmission lines among the members of the pool, under which Kentucky Power would be entitled to payments from the other members for the interstate use of its high voltage transmission facilities based on the full costs thereof. The Commission's order in no way affects the amounts Kentucky Power would be authorized to receive or retain as a result of the FERC proceeding.

the Kentucky Public Service Commission, at the time that Commission decided the prudency of Kentucky Power's purchase, that the Commission had jurisdiction to consider the appropriateness of the acquisition and that such actions did *not* conflict with FERC's authority.

The issue which the petitioners raised in the federal courts below is thus the issue expressly reserved by this Court's decision last term in *Nantahala Power & Light Co.* v. *Thornburg*, 54 U.S.L.W. 4676, 4681 (June 17, 1986), namely whether a state commission properly may adjudicate "the reasonableness of purchasing from a particular source of, rather than paying a particular rate for, FERC-approved power."[6]

There is, therefore, no reason why this Court should now consider whether the federal courts below were correct in abstaining from entertaining petitioner's actions. Kentucky Power submitted all issues as to the prudence of its action in agreeing to the Unit Power Agreement to the Commission and, when it was unsuccessful before the Commission, sought relief in both the state and federal courts. The determination of these issues by the Kentucky state court precludes as a matter of *res judicata* or collateral estoppel relitigation of the issues in the federal courts. *Allen* v. *McCurry*, 449 U.S. 90 (1980); *Kremer* v. *Chemical Construction Co.*, 456 U.S. 461 (1982); *University of Tennessee, et al.* v. *Elliott*, 54 U.S.L.W. 5084 (July 7, 1986); *see* 28 U.S.C. § 1738; *Princess Lida* v. *Thompson*, 305 U.S. 456, 466 (1939).[7]

Even assuming further action in the federal district court is not precluded by *res judicata* or collateral estoppel, FERC has now determined that it will consider the issues petitioners sought to

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[6]"[W]ithout deciding this issue," the Court in *Nantahala Power & Light Co.* "assume[d] that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*." 54 U.S.L.W. at 4681 (emphasis in original).

[7]In Kentucky, the decision of the Franklin Circuit Court is conclusive despite the pendancy of an appeal. *Vaughn's Adm'r* v. *Louisville & N.R. Co.*, 179 S.W. 2d 441, 444 (1944); *see Deposit Bank of Frankfort* v. *City of Frankfort*, 191 U.S. 499, 511 (1903).

raise in the federal district court. Since questions as to the scope of FERC's jurisdiction to take such action and its ultimate interpretation of the Interconnection Agreement are subject to direct appeal to an appropriate federal court of appeals pursuant to 16 U.S.C. § 8251(b), there would, in any event, be no basis for federal district court intervention to consider similar issues. In short, it would in no way advance the resolution of the underlying issues in this proceeding were the Court to grant the petition and, after briefing and oral argument, conclude that the abstention determinations below were erroneous at the time they were made. In all practical terms, the abstention issue in the present case is moot.

2. Nor do the unpublished decisions of the courts below present any general issues of significance as to the application of the much litigated *Younger* and *Burford* abstention doctrines to the factual situation presented, which would conceivably warrant plenary review by this Court. On the contrary, the court of appeals' unpublished decision has little precedential value. Under Rule 24(b) of the Local Rules of the Sixth Circuit, citations of unpublished decisions are "disfavored." Further, the court's decision not to publish its opinion, notwithstanding motions for publication, certainly represents that court's view that the case is without substantial value as a precedent. The Sixth Circuit's Rules include "a presumption in favor of publication of signed and per curiam opinions" and list criteria to be considered by the court in determining whether to publish, which include all of the factors that would give an opinion precedential value.[8]

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[8]Rule 24 of the Local Rules of the Sixth Circuit states in pertinent part:

(a) Criteria for Publication.

(1) It is the policy of the court that the following criteria shall be considered by panels in determining whether decisions will be designated for publication in the Federal Reporter:

> (i) whether it establishes a new rule of law, or alters or modifies an existing rule of law, or applies an established rule to a novel fact situation;
>
> (ii) whether it creates or resolves a conflict of authority either within the circuit or between this circuit and another;
>
> (iii) whether it discusses a legal or factual issue of continuing public interest;
>
> (iv) whether it is accomplished by a concurring or dissenting opinion;

There is, in short, nothing which indicates that the Sixth Circuit considers the several opinions of the panel as representing the definitive views of that circuit as to the scope of the *Younger* and *Burford* abstention doctrines to be followed by it and the circuit's district courts in other situations. And, the possibility that the panel may have erred in its application of the doctrines to the particular circumstances of this case would not itself be a basis for granting the writ even if federal issues allegedly justifying intervention by the federal courts were far more significant than actually is the case here.

3. This Court's determination in *Nantahala Power & Light Co., supra,* of the preemption issue which the Fourth Circuit had abstained from considering in *Aluminum Company of America* v. *Utilities Commission of North Carolina,* 713 F.2d 1024 (4th Cir. 1983), *certiorari denied,* 465 U.S. 1052 (1984), demonstrates that this Court's review of state court determinations of important federal-state issues can lead to an effective and expeditious resolution of such problems and that the Court's review of situations where a federal court of appeals arguably applied abstention doctrines erroneously is not necessary to ensure prompt resolution of major federal-state conflicts. And the even more recent decision of this Court in *Ohio Civil Rights Commission* v. *Dayton Christian Schools, Inc.*, 54 U.S.L.W. 4860 (June 27, 1986), holding that the Sixth Circuit should have applied *Younger* and abstained from ruling on the federal issues presented in that case, since a federal

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(v) whether it reverses the decision below, unless:

(a) the reversal is caused by an intervening change in law or fact, or,

(b) the reversal is a remand (without further comment) to the district court of a case reversed or remanded by the Supreme Court;

(vi) whether it addresses a lower court or administrative agency decision that has been published; or,

(vii) whether it is a decision which has been reviewed by the United States Supreme Court.

(2) Designation for Publication. There shall be a presumption in favor of publication of signed and per curiam opinions. Such opinions shall be designated for publication unless a majority of the panel deciding the case determines otherwise upon consideration of the foregoing criteria. An order shall not be designated for publication unless a member of the panel so requests.

court should not enjoin pending state proceedings "except in the very unusual situation that an injunction is necessary to prevent great and immediate irreparable injury" (54 U.S.L.W. at 4862), clearly indicates that the narrow interpretations of the *Younger* doctrine supported by petitioners here and below are not what the Court intends. Instead, the Court reiterated, with special emphasis, its statement in *Younger* that "the *normal* thing to do when federal courts are asked to enjoin pending proceedings in state courts is not to issue such injunctions" (*ibid*, emphasis in original).

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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September 2, 1986

ADDENDUM

COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION II

84-CI-1760

KENTUCKY POWER COMPANY **PLAINTIFF**

v. **JUDGMENT**

KENTUCKY PUBLIC SERVICE COMMISSION, et al

This appeal is before the Franklin Circuit Court on petition of the plaintiff Kentucky Power Company for review of a rate order issued by the Kentucky Public Service Commission on December 4, 1984. The plaintiff Kentucky Power Company moved this Court for temporary injunctive relief from that order, which motion was denied on February 8, 1985. The case is now before the Court for review of the merits of the Commission's order.

FACTUAL HISTORY

This appeal is merely one installment in a rather lengthy controversy before the defendant Commission. Kentucky Power is a wholly owned subsidiary of American Electric Power Company, Inc. (AEP) and is engaged in the business of supplying electric energy to numerous Kentucky customers. The Kentucky Public Service Commission is vested by Kentucky law with jurisdiction over the company's retail rates.

AEP is a utility holding company and the parent company of numerous utility companies which provide electric energy in several States. The AEP system is a fully integrated interstate utility system.

Beginning around 1978, Kentucky Power sought permission to buy a 15% undivided ownership interest in two large electricity generating plants under construction by Indiana and Michigan Electric (another AEP subsidiary) in Rockport, Indiana. These efforts were not approved by the Public Service Commission or by the Kentucky Appellate Courts.

In September 1981, the Public Service Commission reversed itself and approved Kentucky Power's effort to purchase part of the Rockport plant. On appeal, the Kentucky Court of Appeals reversed that order of the Commission, directing the Commission to make specific findings of fact and to determine other issues. Additional hearings were held by the PSC and again in March 1983, the Commission approved the purchase of a 15% interest in Rockport by Kentucky Power. That decision by the PSC was reconsidered and new evidence was presented to the Commission. On August 2, 1984, the PSC issued a revised order reversing its previous stand and denying Kentucky Power's application to purchase the 15% share of Rockport. That order was not appealed.

Before the last decision by the PSC, Kentucky Power, Indiana and Michigan, and AEP Generating Company entered into a unit power agreement whereby Kentucky Power agreed to buy 15% of the output of Rockport; this agreement represented the financial equivalent of Kentucky Power owning 15% of Rockport. This agreement required the rate approval of the Federal Energy Regulatory Commission (FERC). FERC approved the rates, subject to refund.

As a basis for its decision the PSC had ruled that Kentucky Power could meet its capacity needs by buying surplus power available to it from the AEP power pool. This was possible because the pool had excess capacity, even without the Rockport plant. The PSC concluded that it was cheaper for Kentucky Power to purchase the needed power from the pool under the Interconnection Agreement as opposed to ownership of Rockport. The Commission found that Kentucky Power had a contractual right to purchase from the pool under the Interconnection Agreement.

On December 4, 1984, the PSC ruled that Kentucky Power acted imprudently in entering the unit power agreement to purchase 15% of the power from Rockport when the same amount of power could be purchased under the pool agreement at a substantially lower cost. This ruling was appealed to this Court.

By order of February 8, 1985, this Court denied the plaintiff Company's motion for injunctive relief on the Rockport issue.

Another issue before the Court involves the construction of a transmission line called the Hanging Rock-Jefferson Line. Kentucky Power, along with its sister companies, Appalachian Power Company, Columbus and Southern Ohio Electric, Indiana and Michigan Electric Company and Ohio Power Company, are all members of the AEP system. The AEP system is highly interconnected through utilization of transmission lines.

In 1974, Kentucky Power applied to the Commission for a certificate authorizing construction of a 155 mile transmission line in Kentucky at a cost of $55 million. The transmission line would connect the Hanging Rock substation of Ohio Power Company with the Jefferson substation of Indiana and Michigan Electric Company (Hanging Rock-Jefferson line) and would not have any outlets in Kentucky. Kentucky Power told the Commission that other members of the AEP system would pay for 95% of the line's construction, operation and maintenance costs. A certification was granted on that basis.

In 1983, Kentucky Power told the Commission that the Hanging Rock-Jefferson line would be completed in 1984 at a cost of $123 million and that none of the other members would pay for any of its costs. The Commission then initiated Case No. 8904 to investigate Kentucky Power's need for the transmission line and its cost responsibility.

During the course of that investigation the AEP system filed with the FERC a Transmission Agreement whereby AEP subsidiaries whose investment in transmission facilities was below a specified level would pay rates to those subsidiaries whose investment exceed the specified level. Pursuant to this FERC agreement, Kentucky Power's transmission investment entitles it to receive revenues from its sister utilities; there are no rates to be paid by Kentucky Power.

The Commission's order in Case No. 8904 found that while the Hanging Rock-Jefferson line did provide some reliability benefits to Kentucky Power and its customers under certain extreme conditions of low probability, it was built primarily to enable the system to transfer large quantities of power from Ohio to Indiana,

i.e., bulk power transfers in interstate markets. The Commission further found that the transmission line greatly exceeded Kentucky Power's intrastate needs and consequently, only a portion of the investment should be included in retail rate base. Utilizing an allocation formula similar to the AEP system's allocation of generating capacity under the Pool Agreement, the Commission found that only 44% of the investment in the Hanging Rock-Jefferson transmission should be included in retail rate base and only 44% of the operating and maintenance expenses should be charged to retail customers. Kentucky Power's rates in Case No. 9061 were based on the 44% limitation as ordered in investigative Case No. 8904.

FINDINGS OF FACT

(1) The AEP Interconnection Agreement does not contain any provisions that would require KPC to buy power from the Rockport plant at incremental cost for purposes of meeting Kentucky Power Company's (KPC) internal demand.

(2) The AEP Interconnection Agreement specifically allows KPC to purchase needed power from the AEP pool at the embedded cost of power generated by the pool.

(3) The record in the proceedings before the Public Service Commission clearly demonstrates that it is less expensive to purchase power from the pool than it is to purchase power pursuant to AEP's proposed unit power agreement.

(4) The Unit Power Agreement between AEP Co., and KPC is the equivalent of the purchase by KPC of 15% of the Rockport plant.

(5) In its Order of October 1, 1984, in Docket No. ER 84-579-000, the FERC found that ". . . Kentucky Commission has jurisdiction to consider the appropriateness of KEPC's acquisition of new facilities . . . ," and that there is ". . . no overlap or conflict . . ." between the regulatory roles of FERC and the Kentucky Commission.

(6) In its Order of November 23, 1984, in Docket No. ER 84-579-000, FERC found that State commissions, as well as FERC,

have legitimate concerns ". . . in determining whether purchases reflect prudently incurred expenses for purposes of determining the purchaser's rates for sales to others." FERC further found that ". . . in this proceeding, we do not intend to make or consider any findings concerning KEP Company's prudence in entering the agreement, in light of the availability of alternative power supplies."

CONCLUSIONS OF LAW

(1) PSC acted within its statutory authority in denying recovery of the Unit Power Agreement costs in light of the contractual right of KPC to purchase power at embedded cost from the AEP pool. See *K.U. v. PSC*, Ky. 252 SW 2d 885 (1952)

(2) No confiscation occurs when the PSC rejects for ratemaking purposes excessive or imprudently incurred expenses.

(3) The mere filing of a rate schedule for a Unit Power Agreement with FERC does not preempt the PSC from considering the prudence of KPC in entering into the agreement in light of alternative power supplies, and from denying recovery of excessive costs when they are imprudently incurred.

(4) FERC's interpretation of its authority under the Federal Power Act is entitled to great weight, and sufficient cause to question FERC's interpretation has not been shown.

(5) The PSC Orders complained of are not clearly in conflict with the Federal Power Act.

(6) The Commission's fixing of a value of the Hanging Rock-Jefferson line for retail rate making was just and reasonable and supported by the evidence.

(7) There has been no showing by clear and convincing evidence that the Order of the Commission was unreasonable or unlawful. The Order is supported by substantial evidence in the record.

(8) There is no evidence in the record that the rates set by the Commission are confiscatory.

JUDGMENT

WHEREFORE, the Court ORDERS AND ADJUDGES that the Order of the Public Service Commission in Case No. 9061 is hereby *AFFIRMED* and all relief sought by the plaintiffs herein is *DENIED*.

This is a final and appealable judgment and there is no just cause for delay.

SO ORDERED THIS 21 day of MARCH, 1986.

_____

JUDGE, FRANKLIN CIRCUIT COURT

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

ELECTRIC RATES: Declaratory Order; Consolidation

Before Commissioners: Anthony G. Sousa, Acting Chairman; Charles G. Stalon, Charles A. Trabandt and C. M. Naeve.

Kentucky Power Company) Docket Nos. EL86-10-000 and ER84-579-006

ORDER SETTING ISSUES FOR HEARING AND CONSOLIDATING DOCKETS

(Issued August 20, 1986)

On November 18, 1985, Kentucky Power Company (KEPCO) filed a petition for a declaratory order requesting that the Commission declare the following:

> By virtue of the nature of multi-state power pools in general, and under the specific facts and circumstances that existed when KEPCO entered into the [AEP Generating Company (AEGCO)]/ KEPCO Unit Power Agreement (pending before this Commission in Docket No. ER84-579-001), the American Electric Power System (AEP System) Interconnection Agreement and the AEP System pooling arrangement as it has developed over the years did not permit KEPCO to continue to purchase additional power from the AEP System Pool at average embedded cost rates, and required KEPCO to provide capacity to the Pool, which KEPCO has done through the AEGCO/ KEPCO Unit Power Agreement for Rockport capacity.

Background

KEPCO is a wholly-owned subsidiary of American Electric Power Company, Inc. (AEP), a registered public utility holding company pursuant to the provisions of the Public Utility Holding Company Act of 1935 (PUHCA).[1]

The AEP System operates on an integrated basis pursuant to the terms of the AEP System Interconnection Agreement (System Agreement). While the individual operating companies own and operate the facilities that comprise the AEP System, the facilities are planned on a systemwide basis and operated on central dispatch, generating the lowest cost energy to meet total system load. The System Agreement provides, among other things, for payments among the operating companies to account for capacity deficiencies and surpluses. Monthly cash payments are made by those members which have a "primary capacity deficit," as defined in Article 5 of the System Agreement, to those which have a "primary capacity surplus" at a rate equal to the surplus members' cost of steam capacity.

For many years, KEPCO was a surplus member of the AEP System. However, between the 1978/79 and 1983/84 winter seasons, inclusive, KEPCO's reserve margin declined from 21.0% to −2.3%. In order to obtain capacity, KEPCO had intended to own 15% of the Rockport Generating Station and its output. The Kentucky Public Service Commission (Kentucky Commission), which regulates KEPCO's retail rates, denied the company permission to make the purchase, but then granted the request on rehearing. The Kentucky State courts reversed the Kentucky Commission's decision and remanded the matter for an additional evidentiary proceeding. On remand, the Kentucky Commission affirmed its prior order authorizing the purchase, but limited the investment which could be included in KEPCO's rate base. Subsequently, on August 2, 1984, the Kentucky Commission reversed its decision, again denying KEPCO permission to own a portion of the Rockport plant. As a result, KEPCO entered into a unit power sales agreement with AEGCO providing for the purchase of 15% of the

[1] 15 U.S.C. §§ 79, *et seq.*

output of the Rockport plant.[2] KEPCO then sought to include the costs of this power in its retail rates in lieu of its ownership participation. On December 4, 1984, the Kentucky Commission disallowed KEPCO's purchased power costs associated with the output from the Rockport plant to the extent that it exceeded the cost of power purchased from the AEP System. The Kentucky Commission held that KEPCO could acquire power sufficient to meet its needs under the terms of the System Agreement, and that such purchases would be less costly than purchasing power under the Rockport unit power sales agreement.

In Docket No. ER84-579, this Commission declined to consider the question of whether KEPCO could make purchases under the System Agreement as an alternative to the Rockport purchase. However, that decision was without prejudice to the AEP Companies' filing of a petition for a declaratory order interpreting the System Agreement. KEPCO's present petition is a result of the earlier order.

In support of its petition, KEPCO asserts that the members of the AEP System cannot simply receive the benefits of integrated operations without sharing the burdens or responsibilities. Further, the company argues that each member must supply sufficient capacity to meet its own internal demand plus an adequate reserve margin. While temporary imbalances in capacity among system members may occur, capacity equalization payments are not, KEPCO contends, a substitute for the members' meeting their obligations to provide sufficient generating capacity. The effect of the Kentucky Commission's ruling, KEPCO alleges, would be to require the AEP System to carry a capacity deficient member for an unlimited period of time. KEPCO contends that the Kentucky

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[2]That agreement was docketed as No. ER84-579-000 and filed with this Commission on August 2, 1984. By order issued on October 1, 1984, the Commission suspended the Rockport unit power sales agreement and set the matter for hearing. 29 FERC ¶ 61,002. Subsequently, on February 18, 1986, an offer of settlement was filed resolving all issues but those raised in a request for rehearing of an order issued by the Commission on September 13, 1985. 32 FERC ¶ 61,364. The offer is opposed by the Kentucky Commission. On May 30, 1986, the presiding judge certified the contested offer of settlement. By separate order, the Commission is addressing that request for rehearing.

Commission's order: (1) is contrary to the provisions of the System Agreement, particularly sections 4.2 and 5.7, and the principles which underlie pooling agreements; (2) undermines the Federal Power Act's policy of encouraging voluntary pooling agreements;[3] (3) usurps this Commission's exclusive jurisdiction over wholesale rates; (4) violates the "filed rate" doctrine; (5) results in undue discrimination against the other members of the AEP System; (6) constitutes unlawful "parochial economic protectionism" in favor of Kentucky ratepayers. KEPCO requests expedited consideration of its petition, contending that it is losing $64,000/day ($23 million/year) as a result of the Kentucky Commission's order.

Notice of KEPCO's filing appeared in the *Federal Register*,[4] with comments due, after extension, on or before December 23, 1985. Timely motions to intervene were filed by the Municipal Wholesale Electric Customers of Ohio Power Company (Municipals), the City of Westerville, Ohio (Westerville), the Old Dominion Committee for Fair Utility Rates (Old Dominion), the Attorney General of Kentucky (Kentucky Attorney General), the Indiana Municipal Power Agency (IMPA), the Indiana and Michigan Municipal Distributors Association (IMMDA), the City of Auburn, Indiana (Auburn), Wabash Valley Power Association (WVPA), and the Kentucky Industrial Utility Customers (Kentucky Industrials). In addition, timely notices of intervention were filed by the Public Service Commission of West Virginia (West Virginia Commission), the Kentucky Commission, and the Public Utilities Commission of Ohio (Ohio Commission).

The Municipals, Westerville, Old Dominion, IMMDA, Auburn, WVPA, the West Virginia Commission, and the Ohio Commission do not raise any substantive issues. IMPA requests that the Commission limit its action in this docket to an interpretation of the System Agreement and not institute proceedings pursuant to section 206 of the Federal Power Act[5] as to the justness and reasonableness of the current System Agreement.

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[3]*See* 16 U.S.C. § 824a(a).

[4]50 *Fed. Reg.* 49,094 (1985).

[5]16 U.S.C. § 824e.

The Kentucky Attorney General requests that this Commission decline to issue the declaratory order sought by KEPCO. In support, the Kentucky Attorney General states that the real issue in this case is the wisdom and prudence of KEPCO's agreement to purchase power under the Rockport unit power sales agreement filed in Docket No. ER84-579-000, that the Kentucky Commission has considered KEPCO's rights and obligations under the System Agreement in concluding that KEPCO was imprudent, and, thus, there is no need for this Commission to resolve the question presented. In the event that the Commission determines that interpretation of the AEP System Agreement requires an examination of the actual practices of the AEP operating utilities, the Kentucky Attorney General requests that the Commission set the matter for hearing.

The Kentucky Commission contends that the Commission should decline to issue an order in these proceedings. The Kentucky Commission states that its orders are currently under review in Federal[6] and State[7] court, and that judicial resolution of the controversy between AEP and the Kentucky Commission does not require reference of the matter to this agency. Rather, the Kentucky Commission argues, action by this Commission will serve to delay resolution of the issues. The Kentucky Commission denies that it has usurped this Commission's jurisdiction.

In the event that we do rule on KEPCO's petition, the Kentucky Commission argues that the System Agreement provides that KEPCO may acquire needed capacity at average rates from the other members of the AEP system, and that neither section 4.2 nor 5.7 of the agreement provides to the contrary. The Kentucky Commission characterizes KEPCO's arguments as advancing the proposition that the AEP Companies are not bound by the terms of

[6]*AEP v. Kentucky Public Service Commission*, No. 85-5129 (6th Cir.). On March 24, 1986, the Sixth Circuit affirmed a district court's refusal, on grounds of abstention, to issue an injunction directing the Kentucky Commission to implement KEPCO's requested retail rate increase.

[7]*Kentucky Power Company v. Kentucky Public Service Commission*, No. 84-CI-1760 (Commonwealth of Kentucky, Franklin Circuit Court). On March 24, 1986, the court determined that the System Agreement does not require KEPCO to purchase power under the Rockport unit power sales agreement, rather than under the former agreement, and affirmed the Kentucky Commission's decisions.

their System Agreement. The Kentucky Commission goes on to note that in *American Electric Power Service Corp.*, Opinion No. 50, 8 FERC ¶ 61,068 (1979), *aff'd sub nom. Ohio Power Co. v. FERC*, 668 F.2d 880 (8th Cir. 1982), this Commission approved a capacity equalization charge in the AEP System Agreement based on average investment costs of surplus members, as proposed by AEP, and rejected the trial staff's proposal to calculate the charge based on the costs of the specific generating unit supplying the deficient capacity, *i.e.*, an incremental cost based rate. The Kentucky Commission further argues that the AEP System Agreement does not require that the members maintain a specified amount of capacity relative to their peak requirements. If the AEP Companies are dissatisfied with the terms of the System Agreement currently on file with the Commission, the Kentucky Commission states that they may modify the agreement by filing revisions to it.

On January 9, 1986, the West Virginia Commission filed a statement in support of and adopting the arguments of the Kentucky Commission.

The Kentucky Industrials advance many of the arguments proffered by the Kentucky Commission. In particular, they dispute KEPCO's assertion that the company is obligated to maintain a specific level of generating capacity, either by building it or purchasing the capacity on an incremental cost basis, as opposed to sharing in the AEP System's total capacity and making payments to companies with surplus capacity at average cost. With respect to KEPCO's reliance on sections 5.7 of the System Agreement, the Kentucky Industrials argue that this is misplaced because the provision only covers transactions involving non-affiliated companies.

On January 7, 1986, KEPCO filed an answer to the pleadings of the Kentucky Commission and the Kentucky Industrials. KEPCO states that: (1) section 5.7 (ii) of the System Agreement specifically provides for unit power sales agreements between AEP affiliates; (2) one of the purposes of section 5.7 is to reduce long-term capacity deficits among individual operating companies on the AEP System; (3) the System Agreement embodies commitments to coordinate expansion of power supply facilities as well as system operations; and (4) the Kentucky Commission is obligated

under the "filed rate" doctrine to recognize the full costs incurred by KEPCO associated with the Rockport purchase.

On January 21, 1986, the Kentucky Commission moved that KEPCO's January 6 pleading be rejected as contrary to the Commission's Rules of Practice and Procedure. In the alternative, the Kentucky Commission sought leave to file a reply.[8] The Kentucky Commission contends that section 5.7 (ii) does not refer to either transactions between affiliates or unit sales agreements. With respect to KEPCO's "filed rate" argument, the Kentucky Commission alleges that it is empowered to examine the prudence of KEPCO's entering into the Rockport unit power sales agreement, as recognized in prior rulings by this Commission.

On March 27, 1986, KEPCO lodged copies of the decisions by the Sixth Circuit in *American Electric Power Co., Inc., v. Kentucky Public Service Commission* and the State court in *Kentucky Power Co. v. Kentucky Public Service Commission.* KEPCO states that these decisions demonstrate the urgency of Commission action on its petition for declaratory relief. On April 7, 1986, the Kentucky Commission filed a response. While not objecting to KEPCO's effort to lodge the two court decisions, the Kentucky Commission notes that the Kentucky State court has affirmed its interpretation of the System Agreement. The Kentucky Commission reiterates its view that action by this Commission on KEPCO's petition would serve only to delay, not expedite, resolution of the dispute between the company and the State commission.

Discussion

Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.214), the timely notices and motions to intervene serve to make the Municipals, Westerville, Old Dominion, the Kentucky Attorney General, IMPA, IMMDA, Auburn, WVPA, the Kentucky Industrials, the West Virginia Commission, the Kentucky Commission, and the Ohio Commission parties to this proceeding.

[8]On January 30, 1986, KEPCO filed an answer to the Kentucky Commission's motion to reject. KEPCO states that it does not object to the Kentucky Commission's substantive reply being considered, but insists that KEPCO's January 6 pleading is permitted by the Commission's Rules.

Pursuant to Rule 213(a) of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.213(a)), KEPCO is entitled to file an answer to the motions to intervene. Accordingly, we shall deny the Kentucky Commission's motion to reject KEPCO's January 7, 1986 pleading. Further, construing KEPCO's March 27, 1986 pleading as a motion to lodge, we find good cause to grant that motion in view of the relevance of the two court decisions to this proceeding.

Notwithstanding the request of the Kentucky Commission, we shall not decline to rule on KEPCO's petition. As we explain in greater detail in a companion order also issued today in *AEP Generating Co.*, Docket No. ER84-579-005, in an integrated, affiliated power pool system, such as the AEP System, it may, in effect, be necessary for this Commission to provide its interpretation of power pool obligations and salient rate schedule provisions, where such issues are raised in the context of a jurisdictional system rate filing. An evaluation of the operations of the pool, including the members' capacity obligations and cost sharing arrangements, carries broad interstate implications which are properly considered by this agency. Our decisions regarding wholesale rate schedules, in turn, are conclusive and can compel certain subsidiary effects at the retail ratemaking level. *See Nantahala Power & Light Co. v. Thornburg*, 54 U.S.L.W. 4676 (U.S., June 17, 1986), *citing Narragansett Electric Co. v. Burke*, 119 R.I. 559 (1977). Therefore, we consider it appropriate for KEPCO to seek from this Commission an interpretation of the AEP System Agreement.

KEPCO's petition raises a number of questions involving whether the company is required under the AEP System Agreement to supply sufficient capacity to meet its native load plus a specified reserve margin and, if so, whether the company is obligated (or permitted) to meet the requirement via a unit power sales agreement rather than purchasing capacity at average cost under the terms of the System Agreement.

KEPCO cites various sections of the AEP System Agreement in support of its position, particularly sections 4.2 and 5.7.

Reviewing these two provisions,[9] we find nothing which clearly and expressly requires KEPCO to meet a specified capacity requirement or to enter into a unit power sales agreement as an alternative to purchasing system capacity. However, the AEP System Agreement does evidence an intent, as indicated in section 0.5, that the AEP Companies will engage in coordinated expansion of their power supply facilities. Section 5.7.1 recognizes, as a factor in whether purchases of capacity from non-affiliated companies should be included as primary capacity, the need of capacity-deficient members to rectify such deficiencies, and the interest of all members in maintaining an equalization among the AEP Companies of capacity resources over time. KEPCO's petition for a declaratory order alleges that the AEP Companies' practice has been to rotate generating capacity additions over time among the various members of the system. This is certainly not a unique practice among affiliated power pools, and the parties' individual obligations may not be specifically delineated in a broadly drafted pooling agreement. *See Middle South Energy, Inc., et al.*, Opinion No. 234, 31 FERC ¶ 61,305, *reh'g denied*, Opinion No. 234-A, 32 FERC ¶ 61,425 (1985). *See also* 26 FERC ¶ 63,044 (1984); 30 FERC ¶ 63,030 (1985).

While we recognize the parties' desire to expeditiously resolve their differences, in the interests of cost recovery and continued system planning, we do not believe that the issues are susceptible to summary resolution on the basis of the pleadings. However, we believe that the issues remaining for resolution, which relate to the interpretation of the AEP System Agreement itself and the conduct and practice of the AEP member companies with respect to the planning for and acquisition of capacity, can be expeditiously resolved at hearing. This interpretation would appear to comprise a discrete and primarily factual inquiry:

> Whether the System Agreement, as implemented by the AEP companies, establishes, as KEPCO asserts, an obligation on the part of member companies to supply sufficient capacity to meet

[9]The relevant provisions of the AEP System Agreement are attached in Appendix A.

> their native load requirement over time, or whether such an obligation is inherent in the nature of the AEP system here; or, on the other hand, whether the System Agreement permits a member company to become capacity-deficient, purchasing its capacity shortfall from other members under the System Agreement, on a permanent basis. Given the provisions of the System Agreement itself on this issue, its resolution requires a factual examination of the conduct and practice of member companies in implementing the capacity obligations of the Agreement since its inception. Hence, resolution of this question would appear to involve a primarily factual inquiry, which, while discrete, nevertheless requires a hearing.

As this line of inquiry does not require the presiding judge to resolve the broader, more complex jurisdictional issues presented by the filing, and as the issues relating to the System Agreement interpretation question are clearly defined, discrete and primarily factual, we believe a sufficient record can be developed for their resolution on an expedited basis. Accordingly, we shall direct the presiding judge to complete the evidentiary hearing and to issue an initial decision limited to the interpretation question within 90 days of the date of this order. Subject to this constraint, the presiding judge is, of course, free to set whatever dates he deems appropriate for the completion of discovery, the filing of testimony, the commencement of hearings, and the submission of initial and reply briefs and to take whatever measures for procedural expedition he deems appropriate.

Although the Commission previously declined to consider the matters at issue here in the earlier rate docket involving the Rockport unit power sale, (*AEP Generating Co.*, Docket No. ER84-579), we shall now consolidate these two proceedings in order to preserve all available options for future Commission. We recognize that, in consolidating Docket No. ER84-579-006 with docket other substantial issues could . However, it is not our purpose in consolidating these dockets to expand the scope of this

hearing beyond the interpretation question discussed above. We expressly reserve any future consideration of other potential issues to the Commission pending our review of the record below.

The Commission orders:

(A) The Commission hereby grants KEPCO's March 27, 1986 motion to lodge.

(B) The motion to reject KEPCO's January 7, 1986 pleading is denied.

(C) Pursuant to authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by section 402 (a) of the Department of Energy Act and by the Federal Power Act, particularly sections 205, 206, and 306 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R., Chapter I), a public hearing shall be held concerning the interpretation of the AEP System Agreement consistent with the body of this order.

(D) A presiding administrative law judge, to be designated by the Chief Administrative Law Judge, shall convene a conference in this proceeding to be held within fifteen (15) days from the date of this order in a hearing room of the Federal Energy Regulatory Commission, 825 North Capitol Street, N.E., Washington, D.C. 20426. Such conference shall be held for purposes of establishing a procedural schedule, including the submission of a case-in-chief by KEPCO. The presiding judge is hereby directed to complete the proceeding on the interpretation of the AEP System Agreement and to issue an initial decision within 90 days of the date of this order. The presiding judge is authorized to establish procedural dates and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

(E) Subdocket 000 in No. EL86-10 is hereby terminated. The evidentiary hearing ordered herein is assigned Docket No. EL86-10-001.

(F) Docket Nos. EL86-10-001 and ER84-579-006 are hereby consolidated for purposes of hearing and decision.

By the Commission.

(S E A L)

Kenneth F. Plumb,
Secretary.

APPENDIX A

Selected Provisions of the AFP System Interconnection Agreement

0.5 WHEREAS, the Members through cooperation with each other have been successful for some years in achieving substantial economies in the conduct of their business by coordinating the expansion and operation of their power supply facilities.

4.2 The Members agree that their electric power sources, which shall include all the generating stations owned by the Members and all electric power available to them through interconnection with affiliated companies other than Members and Foreign Companies, shall be used as needed to carry the combined load obligations of the Members under the direction of the Pool Manager. Each Member in return shall receive at all times sufficient electric power and energy from such sources to meet the specific load obligations of such Member.

5.7 MEMBER PRIMARY CAPACITY—The aggregate capacity of the electric power sources of a particular Member, in Kilowatts, that is normally expected to be available to carry load. Such capacity shall include (i) the capacity installed at the generating stations owned by the Member and (ii) the capacity available to that Member through interconnection arrangements with affiliated companies or Foreign Companies, if so designated by the Operating Committee with approval of the Members.

5.7.1 All determinations by the Operating Committee pursuant to (ii) of Section 5.7 with respect to purchases of capacity from non-affiliated companies shall take into account, but shall not be limited to, the following circumstances and consideration: (1) the term during which such capacity will be available, a commitment from a reliable source of power and energy for at least five years being normally regarded as appropriate for inclusion as a capacity source of a particular Member, with purchases of a short or inter-

mediate duration being normally regarded as System purchases under Article 7; (2) whether the availability of the purchased capacity will be comparable to the availability of the installed primary capacity of the Members, although the Operating Committee may make adjustments in the quantity of purchased capacity to be included as Member Primary Capacity to give effect to any disparity in the availability of such purchased capacity; (3) the need on the part of a member with a Member Primary Capacity of an extended nature to rectify or alleviate such deficit and the interest of all Members in maintaining an equalization among the Members of capacity resources over a period of time.

5.7.2 In the event that arrangements are made hereunder for any Member to make capacity available to an affiliated company or to a Foreign Company through the sale of such Member, for its own account, of unit capacity or other non-firm capacity, the amount of the capacity so sold shall be excluded from the Primary Capacity of such Member.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

ELECTRIC RATES: Rehearing: Jurisdiction; Prudence; Clarification

Before Commissioners: Anthony G. Sousa, Acting Chairman; Charles G. Stalon, Charles A. Trabandt and C. M. Naeve.

AEP Generating Company) Docket No. ER84-579-005

ORDER ON REHEARING

(Issued August 20, 1986)

On October 11, 1985, AEP Generating Company (AEGCO), Indiana & Michigan Electric Company (I&M), and Kentucky Power Company (KEPCO) (collectively, the AEP Companies) filed a request for rehearing of the Commission's order issued on September 13, 1985 in these proceedings. 32 FERC ¶ 61,364. By order issued on November 12, 1985, the Commission granted rehearing for the limited purpose of further consideration.

Background

The Rockport Generating Station consists of two 1300 MW units located in Spencer County, Indiana. I&M and AEGCO each own 50% of the plant. Pursuant to the terms of unit power sales agreements filed in this proceeding, AEGCO sells to I&M and KEPCO 35 percent and 15 percent, respectively, of the total capacity of Rockport Unit No. 1. By order issued on October 1, 1984, the Commission, *inter alia*, accepted AEGCO's agreements of filing, suspended them to become effective, subject to refund, on the initiation of commercial operation of the unit, and set the agreements for hearing. 29 FERC ¶ 61,002. On rehearing of the October 1, 1984 order, the Commission ruled that it did not intend to make or consider any findings concerning KEPCO's prudence in light of the availability of alternative power supplies in entering into the Rockport unit power sales agreement. 29 FERC ¶ 61,246,

p. 61,501 (issued November 23, 1984). Subsequently, on December 21, 1984, the AEP Companies filed a motion for clarification or, in the alternative, for rehearing of the November 23, 1984 order. Specifically, the AEP Companies requested that the Commission state that it would consider evidence regarding the interpretation of the AEP System Interconnection Agreement or grant rehearing insofar as it intended to preclude consideration of the AEP System Interconnection Agreement. By order issued on September 13, 1985, the Commission denied the AEP Companies' motion without prejudice to their filing a petition for a declaratory order as to the interpretation of the AEP System Interconnection Agreement.[1]

In their request for rehearing, the AEP Companies allege that the Commission erred in three respects. First, the AEP Companies assert that the Commission did not rule upon their alternative request to grant rehearing of the November 23, 1984 order in the event that the order was not interpreted in the manner proposed by the AEP Companies. Second, the AEP Companies allege that the Commission did not state with sufficient clarity its views regarding the relationship between State and Federal jurisdiction. Third, the AEP Companies contend that the Commission's ruling is inconsistent with its decision in *Middle South Energy, Inc., et al.*, Opinion No. 234, 31 FERC ¶ 61,304, *reh'g denied*, Opinion No. 234-A, 32 FERC ¶ 61,425 (1985).

Discussion

With respect to the first issue raised by the AEP Companies, they are incorrect in suggesting that the Commission did not rule upon their request, in the alternative, for rehearing in the September 13 order. The AEP Companies' motion alleged, in support of

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[1]Subsequently, on November 18, 1985, KEPCO filed a petition for a declaratory order in Docket No. EL86-10-000 requesting that the Commission interpret the AEP System Interconnection Agreement on the points raised by the AEP Companies.

their request, that the Commission erred by refusing to permit consideration of whether alternatives to the Rockport unit power sale agreement existed or to interpret the AEP Interconnection Agreement. The effect of these rulings, the AEP Companies alleged, would be that the Kentucky Public Service Commission (Kentucky Commission), which possesses jurisdiction over KEPCO's retail rates, would usurp this Commission's authority over the AEP System Interconnection Agreement (*See* Motion to Clarify Order or, in the Alternative, Application for Rehearing, pp. 13-14). In response to the AEP Companies' motion, the September 13 order specifically addressed these points and denied their motion. They are incorrect in their assertion that the Commission overlooked their rehearing request. Nonetheless, as discussed below, we are now persuaded that rehearing is warranted, to the extent of clarifying our views concerning the relationships between the AEP agreements and the appropriate interpretive role of this Commission.

In the September 13, 1985 order, the Commission discussed the respective jurisdiction of this Commission and of State commissions regarding interpretation of wholesale rate schedules. The order stated:

> We agree . . . that we do not necessarily have *exclusive* jurisdiction with respect to the interpretation of filings tendered to the Commission pursuant to the Federal Power Act. However, we also note that this Commission must have primary jurisdiction to decide questions on the interpretation and application of contracts and rate schedules within our exclusive jurisdiction. Therefore, once we have decided such a question of interpretation, a State commission is bound to follow that decision. (Emphasis supplied).

32 FERC at 61,821.

The AEP Companies allege that this passage is capable of three interpretations. First, it could be interpreted to mean that the Kentucky courts and Kentucky Commission would defer to this

Commission for an interpretation of the AEP Interconnection Agreement before they decide whether KEPCO was prudent in entering into the Rockport unit power sales agreement. Then, the State court or commission is bound to follow this Commission's interpretation. Second, the AEP Companies suggest, the Commission's order might mean that States may interpret only those portions of wholesale rate schedules and contracts which bear on local matters. Third, the September 13 order might provide that the States may interpret any portion of a wholesale rate schedule or contract, but only until this Commission speaks, at which time our interpretation would preempt the State interpretation.

The AEP Companies also contend that the Commission, in stating that interpretation of the AEP System Agreement is not relevant to the determination of the justness and reasonableness of the Rockport unit power sales agreement, has taken an overly restrictive view of its task. The AEP Companies contend that in order to find the Rockport agreement just and reasonable, the Commission must determine that a lower, embedded cost rate is not available to KEPCO. Further, the AEP Companies contend that the Commission's view is contrary to the role taken by it in Opinion No. 234. In that case, the Commission determined the proper allocation of a new plant's costs among the members of an integrated holding company system, given the history of capacity additions on the system.

Although we do not concur fully with the position of the AEP Companies, we agree, upon further reflection, that rehearing is warranted. The AEP System is an integrated public utility holding company system, organized pursuant to the provisions of the Public Utility Holding Company Act of 1935 (PUHCA).[2] Both the Rockport unit power sales agreement and the AEP System Interconnection Agreement are subject to the exclusive jurisdiction of this Commission under the Federal Power Act. Clearly, this Commission, and only this Commission, has the authority to determine just and reasonable allocations of costs and rates among the members of an integrated interstate system. *American Electric Power*

[2]15 U.S.C. §§ 79, *et seq.*

Service Corp., 32 FERC ¶ 61,363, 61,817-18 (1985); *Cf.*, *Nantahala Power & Light Co. v. Thornburg*, 54 U.S.L.W. 4676 (U.S., June 17, 1986). In Opinion No. 234, for example, we determined how the investment cost of the Grand Gulf Nuclear Unit No. 1 should be allocated among the operating utilities of the Middle South System in light of the history of plant additions and other operational aspects on the system. We believe that the present controversy is factually similar, although revisions to the AEP System Agreement are not now before us, as was the situation with respect to the System Agreement in *Middle South.*

We recognize that the November 23, 1984 order in this proceeding stated that the prudence of KEPCO's decision to enter into the Rockport agreement, in light of the availability of alternative power supplies, was not an issue. The Commission stated that it did not view its responsibilities under the Federal Power Act as including a determination that a purchaser had acted wisely, but that the question was a legitimate concern when the purchaser sought to pass through costs associated with the transaction in its rates for sales to others. 29 FERC at 61,501. Under narrow, non-pool circumstances, that view would remain sufficient and dispositive. That opinion was expressed in this case because a discrete rate filing was before the Commission, not a request to modify the broad, underlying pooling agreement. In that context, the salient inquiry was considered to be the validity of the cost support for the Rockport unit charges, not the availability of other power alternatives. Indeed, this is the typical basis for evaluating the reasonableness of a filed unit rate, since potential alternatives may exist with respect to any filed rate. The continuing controversy that has ensued, however, makes it clear that where, as here, the transaction involves affiliated, jurisdictional utilities, which are members of an integrated, interstate holding company arrangement, performing diverse functions on a coordinated basis, and particularly where differing interpretations are advocated concerning the parties' rights and obligations under the basic system agreements, the relevant issues may not be so readily segregated. Under these circumstances, more complex, interrelated questions arise and, whether one characterizes the questions as related to prudence, interpretation, or cost allocation, they are clearly matters most appropriately resolved by this Commission as part of its overriding

authority to evaluate and implement all applicable wholesale rate schedules. Given that the implications of the parties' obligations under the System Agreement have been raised in the context of determining the justness and reasonableness of the unit power sales arrangement (as well as the rates), the Commission will undertake to interpret the System Agreement in that context. Insofar as such an interpretation determines or affects the appropriateness and reasonableness of the unit power sales agreements, we consider our interpretation to be conclusive. *See Nantahala Power & Light Co., supra.*

In retrospect, it appears that the Commission could have considered questions regarding the parties' entitlements under the AEP System Interconnection Agreement in the present docket, although this inquiry would have been separate from the narrower evaluation of the cost basis for the Rockport unit power rates. However, largely at the suggestion of the Commission, KEPCO has separately requested a declaratory order concerning its ability to purchase needed capacity at average embedded cost under the System Agreement, as an alternative to the Rockport purchase, in Docket No. EL86-10-000. That proceeding now provides a suitable vehicle for considering the parties' positions regarding the capacity obligations of the system members, the availability (and appropriateness) of system power sales to KEPCO, as an alternative to a unit power purchase from Rockport, as well as any appropriate remedies.[3] A separate order addressing these questions in Docket No. EL86-10-000 is being considered concurrently by the Commission. That order will consolidate these proceedings for further Commission inquiry and any remedial action.

In light of the above, we shall clarify the September 13, 1985 order and grant rehearing as indicated in the body of this order.

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[3]We note that there are, and have been, a variety of procedural options available for a party to solicit such an interpretation. For example, the utilities or any affected State commission could have requested a declaratory order as soon as a disagreement became evident.

The Commission orders:

(A) The AEP Companies' request for rehearing is hereby granted and the Commission's order of September 13, 1985, is hereby clarified to the extent discussed in the body of this order.

(B) Subdocket 005 of Docket No. ER84-579 is hereby terminated. Further proceedings herein shall be held in Docket No. ER84-579-006.

By the Commission.

(S E A L)

Kenneth F. Plumb,
Secretary.